ZCL COMPOSITES INC. ANNUAL REPORT 2004

Setting a Higher Standard

Corporate Profile

Established in 1987, ZCL has grown to become Canada's leading supplier of fiberglass liquid storage systems. An unrelenting drive to manufacture superior products that "simply will not corrode" has made ZCL the preferred choice in many market sectors. The Company developed Canada's first double wall fiberglass tank and continues to innovate with expanding product lines for many applications. ZCL remains committed to quality products, continually setting a higher standard for economical, environmentally-safe and long-lasting liquid storage technology.

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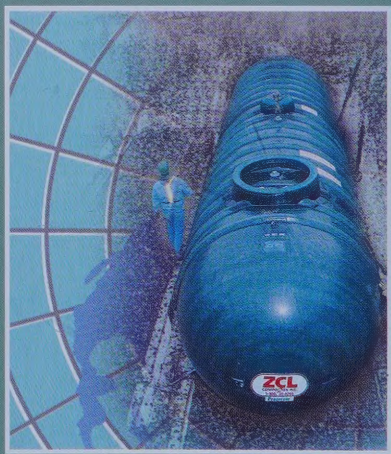
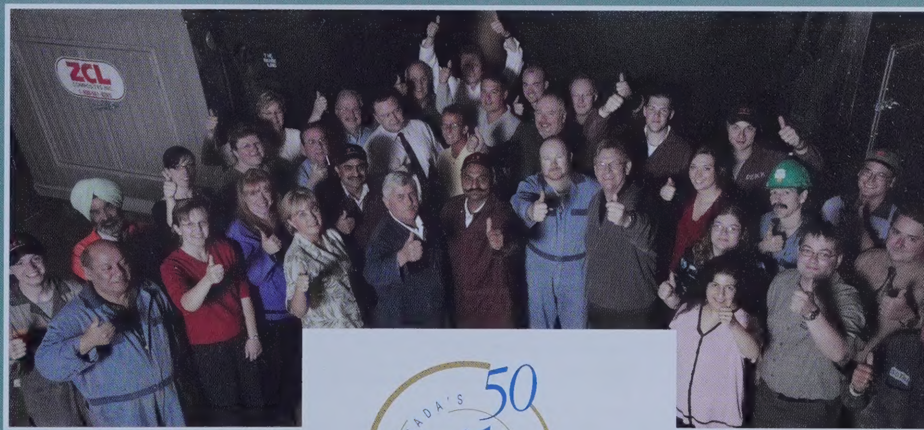


Annual Report

Our Mission – to provide global solutions for environmentally-safe storage of petroleum products and other liquids

Setting a Higher Standard

In January 2004, we were honoured to be recognized as one of Canada's 50 Best Managed Companies. This prestigious award is shared with and celebrated by the whole of our organization.



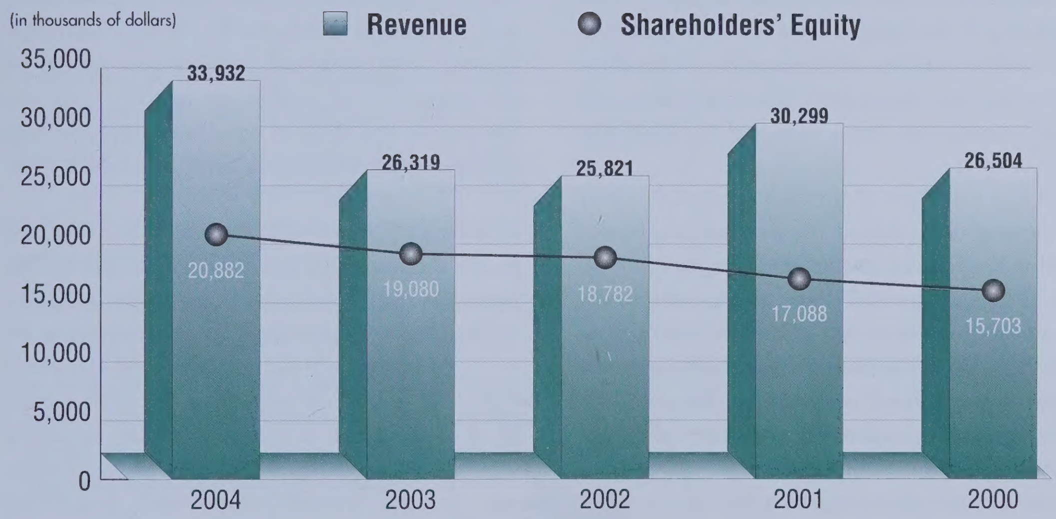
CANADA'S 50 BEST MANAGED COMPANIES

2004

Financial Highlights

In thousands of dollars, except share information	2004	2003	2002	2001	2000
Statements of Income					
Revenue	33,932	26,319	25,821	30,299	26,504
Restructuring and license litigation costs (note 1)	-	-	98	936	3,582
Net income (loss) from continuing operations (note 2)	1,952	756	1,836	1,534	(895)
Net income (loss) from discontinued operations (note 3)	-	-	-	-	(225)
Net income (loss) for the year	1,952	756	1,836	1,534	(1,120)
Convertible subordinated debenture costs, net of tax (note 4)	-	(461)	(815)	(718)	(661)
Basic and diluted earnings (loss) per share	$0.11	$0.02	$0.11	$0.09	($0.19)
Statements of Cash Flows					
Cash flows from continuing operations (note 3)	6,101	3,435	2,464	5,048	(281)
Purchase of property, plant and equipment	581	455	155	528	424
Balance Sheets					
Working capital (note 5)	10,099	8,669	7,863	4,827	2,402
Total assets	26,467	28,014	24,489	26,080	29,292
Long-term debt (including current portion)	-	4,643	1,912	2,634	3,353
Shareholders' equity (note 6)	20,882	19,080	18,782	17,088	15,703
Common shares, ending	17,511,320	17,716,920	9,295,866	9,295,866	9,295,866

Management considers the above earnings and other measures to be meaningful indicators of the financial position, results of operations and cash flows of the Company. Readers are cautioned that some of these measures may not have standardized meanings prescribed by Canadian generally accepted accounting principles, and are therefore not readily comparable to, and may be different than the calculations of, similar measures provided by other corporations.



Note 1 – Restructuring and license litigation costs were legal, occupancy and other costs related to the litigation with Xerxes Corporation in the USA, the review of operations and dispute with ZCL-USA, Inc., the shutdown of the Belleville, Ontario plant, and management restructuring. These costs were not considered to be part of the ongoing operations and not expected to recur in the future, and were separately disclosed in the Statements of Income in the consolidated financial statements.

Note 2 – Goodwill charges were deducted in 2001 and 2000 before the change in accounting policy in 2002 whereby goodwill is not amortized.

Note 3 – Discontinued operations in 2000 related to the discontinuance and sale of distribution operations.

Note 4 – Convertible subordinated debenture costs, net of tax, were charged directly to retained earnings (deficit) and deducted for purposes of determining basic and diluted earnings per share.

Note 5 – Working capital is calculated as current assets less current liabilities recorded on the balance sheets.

Note 6 – Shareholders' equity included the equity portion of the convertible subordinated debenture prior to repayment in September 2002.

Message to Shareholders

"setting a higher standard"

We are pleased to report revenue for the year ended March 31, 2004 increased by 28.9% to a record $33.9 million. Net income increased by $1.2 million for the year, to a record $1,952,000, and basic and diluted earnings per share increased by $0.09, to $0.11 in 2004.

The increase in net income this year was due to the higher revenue, plus a recovery of prior years' income taxes of $145,000, or $0.01 per share, in the fourth quarter. However, net income in 2004 was reduced by $880,000 ($580,000 after tax, or $0.03 per share) in the second quarter by the provision for impairment of the agreement receivable from ZCL Enviro Systems, Inc. We are taking all actions available to recover the amounts outstanding, and any future recoveries will have a positive effect on our financial results.

Revenue in fiscal 2004 was higher than 2003 in each quarter, except for the second quarter where completion and shipment of a number of large orders were delayed to early in the third quarter. The first, third and fourth quarters of 2004 were each record quarters. Activity in the downstream and upstream sectors of the petroleum industry, as well as other traditional markets, was strong throughout 2004. Products we introduced in recent years – home heating oil tanks, Protektor® and Pinnacle™ oilfield tanks, filament wound pressure vessels, as well as custom storage and lining systems – continue to gain market acceptance and contribute to revenue.

Our success is based on our customers and the principles that guide them. We have alliance agreements and long-term contracts with many of our key customers, and subsequent to March 31, 2004, two major contracts were announced. Contracts such as these are an expression of confidence in ZCL, and our commitment and ability to consistently supply the high quality products and services that our customers value.

In January 2004, we were honoured to be recognized as one of Canada's 50 Best Managed Companies. This prestigious award is shared with and celebrated by the whole of our organization. To commemorate the contributions of our team, we issued 100 shares to each of our employees. Our team remains committed to quality products, constantly setting a higher standard for economical, environmentally-safe and long-lasting liquid storage technology.

Last year, we targeted annual growth in revenue of 15% to 20%, along with a corresponding increase in income. We are pleased to have achieved and surpassed this goal in fiscal 2004, and are now poised and confident that we can continue to reach this target.

Our growth strategy to date has taken us to the current level of revenue approaching $34 million. Some of the successes that we have achieved to this point are:

- developed a proven tank design utilizing the best technology available in the world;
- introduced our products on a national basis, so that they could be accepted by our major customers as part of their overall tank upgrade programs;
- provided the best value in the marketplace, by supplementing the basic product with features,

"Our growth strategy to date has taken us to the current level of revenue approaching $34 million."

accessories, warranties, and volume discount programs;

- embarked on a program of strategic alliance arrangements with core customers and suppliers;
- increased the value of underground products through a unique and exclusive extended-warranty program, providing insurance coverage against environmental pollution;
- acquired additional tank manufacturing and other capability in key areas of the Canadian marketplace;
- realized cost reductions and improved manufacturing quality with the implementation of certified ISO quality assurance and continuous improvement programs throughout the organization;
- expanded key tank markets and developed new products where existing technology could be used to maximum advantage, including a proprietary line of custom-manufactured, aboveground storage systems;
- acquired the technology and production facilities of Parabeam, an integral input in double wall tank manufacturing and lining;
- developed proprietary technology for double wall lining materials and processes to improve the safety, quality and profitability of tank lining systems; and
- acquired manufacturing capability and expertise in tank lining techniques and field service and aboveground products.

With a sound strategy, proven capabilities and focused commitment, we are well positioned for the next phase of our growth. We have targeted the aboveground and tank lining markets. The acquisition of the business assets of Durex Steel & Alloy Industries Ltd. allows us to access the retail aboveground tank market which has eluded us until now. We can expand tank manufacturing and lining operations and offer a full line of products to our existing alliance customers as well as to new customers.

We are focused on the development of our tank lining technologies, and are on schedule to commence field trials during the second half of fiscal 2005. Tank lining is a very large and lucrative international market and, at this time, there are no competitive alternative products in the marketplace. Customers are the same, and require the same type and level of service used to supply our current liquid storage system products. By using familiar technology adapted from double wall tank manufacturing processes and leveraging our core competencies, product development is less risky and our customers can be assured that they are getting a reliable and proven product. We can control all the key components of this new technology through patents, proprietary products and processes, and in-house technical expertise.

This has been an exciting year. I am very grateful for the continued counsel of our Board of Directors, for the outstanding efforts of our team of more than 175 employees across the country and abroad, and for the patience and trust of our shareholders. With the support of our dedicated customers, employees, and shareholders, we will continue to deliver quality products to the market and create value for our shareholders.

Venence G. Côté
President and Chief Executive Officer
May 2004

Business Overview

Overview of the Liquid Storage Market

The storage of liquids, especially hazardous goods, covers a broad spectrum of applications and industry sectors, and includes both underground (UGST) and aboveground (AGST) storage systems. Some of the industry sectors are:

Petroleum:

- Production (upstream) (largely Western Canada);
- Distribution (midstream);
- Retail (downstream);

Industrial:

- Transportation (including trucking, airports, shipping and marine, and government);
- Chemical and petrochemical;
- Forestry, pulp and paper;
- Mining;
- Aquaculture and fisheries;
- Agriculture;

Infrastructure and domestic:

- Home heating oil (largely Eastern Canada and North-Eastern USA);
- Water and water treatment;
- Sewage storage and treatment;
- Municipal, commercial and residential infrastructure.

Many factors drive the demand for liquid storage products, including industry specific conditions and trends. For example, some of the factors in the petroleum industry include:

- increased environmental legislation, standards and awareness;
- the replacement, or requirement for secondary containment and monitoring, of ageing and leaking tanks;
- demographic changes which result in relocation of retail gasoline outlets;
- design modifications and marketing trends that lead to changes in sites, configurations and locations;
- storage requirements for new fuels and additives;
- new entrants to retail and other markets; and
- economic conditions in the industry, including commodity prices and drilling activity.

Liquid storage systems are generally made of fiberglass reinforced plastic (FRP), steel, and a number of combinations and variations including cathodically-protected steel, composite steel coated, and jacketed or lined steel. The underground tank market (new installations and replacements) is dominated by FRP products, while the aboveground tank market is largely served by steel products. For certain aboveground applications, such as the retail (downstream) market, standards and regulations specify steel-based storage products.

"There is a large and growing market for the replacement or upgrade of both underground and aboveground liquid storage systems."

There is a large and growing market for the replacement or upgrade of both underground and aboveground liquid storage systems. This demand is driven by ageing (and leaking) tanks, and by environmental legislation and industry standards governing system design, installation, monitoring, and locations, as well as new types of fuels and materials. At present, there are no fully-compliant, competitive alternatives to achieve these upgrades, without the requirement for costly replacement.

ZCL's Core Business and Vision

ZCL's core business is the manufacture and distribution of liquid storage systems, including fiberglass underground and aboveground storage tanks and related products and accessories. The vision is to be the leading global provider of environmentally-friendly liquid storage solutions.

The Company has demonstrated innovative industry leadership and has kept pace with the changing needs of the marketplace through:

- leading-edge technology, providing superior, cost-effective products;
- best-in-class engineering and manufacturing capability;
- a national production and service network;
- customer-focused marketing and product development, resulting in long-term customer alliances; and
- a strong organization and processes to support success and growth.

ZCL was incorporated in 1987 under the Canada Business Corporations Act, and has grown to become Canada's leading supplier of liquid storage systems. An unrelenting drive to provide solutions to meet the needs of customers, and to manufacture superior products that "simply will not corrode", has helped make the Company the preferred choice in many industrial, consumer and retail sectors. ZCL remains committed to continue to set the standard for economical, environmentally-safe and long-lasting liquid storage technology.

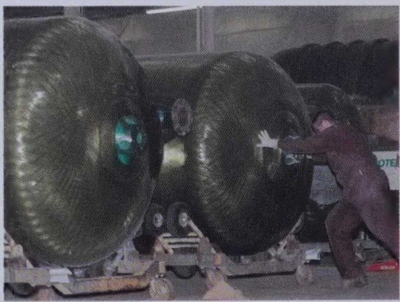
The Company has led the way in innovative fiberglass tank technology, from the Underwriters' Laboratories of Canada (ULC) listed single wall storage tank in 1988, to the development and introduction of the first double wall tank manufactured in Canada. The Prezerver® system and other product innovations, such as the Protektor® aboveground tank, have a high level of industry acceptance. Using the same proven technology and manufacturing expertise, a number of new products have been recently successfully introduced into several market sectors. The Company continues to innovate with expanding product lines for many applications and industries, including double wall tank upgrade systems and aboveground products to compete in markets traditionally served only by steel tanks.

ZCL markets its tank and lining products under the Greentank®, Protektor®, and Everlast™ trademarks, and combines tanks and related products under the Prezerver® trademark for complete liquid storage systems carrying a $2 million insurance-backed warranty against pollution for a period of ten years.

Business Overview continued

Substantially all business activities are presently carried out in Canada. The Company's major markets are the retail (downstream) and production (upstream) sectors of the Canadian petroleum industry, with combined revenue from these sectors comprising approximately 80% of total revenue. Similar liquid storage solutions and products for various other sectors, including home heating, chemical, transportation, and aquaculture, make up the remaining portion of the Company's revenue.

ZCL continues to expand into global markets. In the United States, the Company supplies aboveground storage and tank lining systems to the petroleum, home heating oil, aquaculture, and other industrial markets. The Company, through its subsidiary, Parabeam Industries BV, also markets a three-dimensional glass fabric to various industrial and commercial markets – transportation, marine, construction and other industrial corrosion markets – in Europe and Asia, as well as North America. ZCL Enviro Systems, Inc., through a license agreement with the Company, sells to petroleum and industrial markets in the Philippines.



Oilfield Pressure Vessels

ZCL's Line of Products

The Company's products include FRP underground tanks, FRP aboveground tanks, FRP-lined steel tanks, steel aboveground storage systems (with the acquisition of the assets of Durex Steel & Alloy Industries Ltd. in May 2004), FRP tank lining systems, and related products, services and accessories, as well as the Parabeam three-dimensional glass fabric.

ZCL's traditional and main products are underground storage systems for the retail petroleum market. The Company has approximately 90% of the Canadian major and independent oil company market, most of which have adopted ZCL's technology as the standard for their underground retail networks. Historically, the second and third quarters of the Company's fiscal year have the highest levels of activity, corresponding to the seasonality of the installation of underground liquid storage systems in Canada.

Aboveground storage systems comprise a significant portion of both the production (upstream) and retail (downstream) tank markets. The Company introduced a number of aboveground tank products over the past several years, using the same proven technology and manufacturing expertise. While ZCL currently only has a small portion of this market, these products, including Protektor® tanks for the production sector, are achieving a high level of industry acceptance.

Subsequent to March 31, 2004, the Company acquired the business assets of Durex located in Edmonton, Alberta. Durex manufactures steel aboveground storage tanks, including double wall ULC-listed products for the retail petroleum industry, and custom steel tanks for the upstream petroleum and other markets. Durex was a supplier of steel AGST to the Company, for use in the production of FRP-lined storage systems.

"Secondary containment, or double wall lining, of both aboveground and underground systems is a growing market and an emerging product for the Company."

This acquisition allows the Company to access the retail AGST market which is served by steel-based products. Tank manufacturing and lining operations can be expanded, and a full line of products can be offered to existing alliance customers as well as to new customers.

Secondary containment, or double wall lining, of both aboveground and underground systems is a growing market and an emerging product for the Company. FRP-lined steel tanks, and corrosion protection and coating systems, are presently supplied to meet some of the market needs. The further development of new FRP lining materials and processes, that will deliver superior quality and performance and inherently safe installation techniques, will allow the Company to exploit the tremendous market opportunities. These new lining systems, utilizing the Company's proprietary technology, will feature secondary containment with leak detection and monitoring capability at competitive prices.

Another significant aboveground market that was developed by the Company is the home heating oil sector. Furnace oil is used for heating in about 8 million households in North America (largely Eastern Canada and North-Eastern USA). Traditional fire and storage regulations dictated that home heating oil storage tanks be made from steel. A growing concern is leaking tanks and the resulting environmental, property and liability problems. The Company surpassed industry standards and regulations, and introduced an FRP product, offering a new level of security for home owners (and insurance companies and lenders).

Other products of the Company, which generate increasing sources of revenue, are:

- the horizontal Protektor®II and vertical Pinnacle™ tanks for the safe storage of produced water, in response to the trend to aboveground low cost storage, and new industry and government guidelines, in the upstream market;
- filament wound pressure vessels for above-ground or underground (direct burial) storage of corrosive produced water and liquids from flare stacks;
- oil-water separators, to meet increasingly stringent regulations regarding water and waste-water treatment from run-off streams, as well as many other applications for the separation of oil from water;
- water and sewage holding and treatment systems, to meet the environmental needs of growing markets in rural areas, new housing developments, and recreational and municipal facilities;
- custom products in many industries, such as aquaculture, marine, agriculture, petrochemical, and pulp and paper, to meet a wide variety of long-lasting, safe storage and corrosion-prevention applications, and environmental regulations; and
- fiberglass restoration, roof systems and coating systems, to meet the corrosion protection needs in various industries.

Management's Discussion and Analysis

May 21, 2004

The following discussion and analysis should be read in conjunction with the audited consolidated financial statements of the Company for the years ended March 31, 2004 and 2003, and the notes relating thereto, as well as the Message to Shareholders and other management discussion included in this Annual Report. Financial statements are prepared in accordance with Canadian generally accepted accounting principles, and all amounts are in Canadian dollars unless otherwise indicated.

This report includes forward-looking statements that are based on current expectations and are subject to risks and uncertainties. Many internal and external factors may cause actual results to differ materially, including, but not limited to, those outlined in Risks and Uncertainties below. The Company disclaims any intention or obligation to update or revise any such forward-looking statements, whether as a result of new information, future events, or otherwise.

OVERALL PERFORMANCE

The Company operates in one reportable segment, which is the manufacture and distribution of liquid storage systems, including fiberglass underground and aboveground storage tanks and related products and accessories. Historically, the second and third fiscal quarters have the highest levels of activity, corresponding to the seasonality of the installation of underground liquid storage systems in Canada.

Everlast™ Double Wall Tank, Nisku Plant

Revenue in 2004 increased by 28.9% to a record $33.9 million, from $26.3 million in 2003. Net income increased by $1.2 million, to a record $2.0 million from $756,000 in 2003. Basic and diluted earnings per share increased by $0.09, to $0.11 from $0.02 in 2003.

The general trend of increasing revenue began in the third quarter of fiscal 2003, and continued throughout fiscal 2004. Revenue in 2004 was higher than 2003 in each quarter, except for the second quarter where completion and shipment of a number of large orders were delayed to early in the third quarter. The first, third and fourth quarters of 2004 were each record quarters.

Activity in the downstream and upstream sectors of the petroleum industry, as well as other traditional markets, was strong throughout 2004. Products introduced in recent years – home heating oil tanks, Protektor® and Pinnacle™ oilfield tanks, filament wound pressure vessels, as well as custom storage and lining systems – continue to gain market acceptance and contribute to revenue.

The increase in net income in 2004 was due to the higher revenue, plus a recovery of prior years' income taxes of $145,000, or $0.01 per share, in the fourth quarter. However, net income in 2004 was reduced by $880,000 ($580,000 after tax, or $0.03 per share) in the second quarter by the provision for impairment of the agreement receivable from ZCL Enviro Systems, Inc. ("Enviro").

"A current focus is the development and marketing of the tank lining technologies, as well as other new products."

Net income in 2003 was negatively impacted by losses incurred by Mocoat Services Incorporated ("Mocoat") and Parabeam Industries BV ("Parabeam"), purchased during that year, as steps were taken to integrate those operations into the overall liquid storage business.

Earnings per share in 2003 were reduced by $0.03 (2004 – nil) due to the costs, net of tax, of the convertible subordinated debenture ("debenture"). The debenture was repaid in September 2002 and these costs were eliminated. During fiscal 2004, all long-term debt was repaid.

Cash flows from operating activities increased by $2.7 million, to $6.1 million in 2004 from $3.4 million in 2003, commensurate with the increase in income before amortization, provision for impairment of agreement receivable and future income taxes.

A current focus is the development and marketing of the tank lining technologies, as well as other new products. The Company is working with customers and suppliers to develop new lining materials and processes in order to deliver a product with superior quality and performance, along with inherently safe installation techniques. Product development costs of $141,000 were deferred in 2004. This product development continues with field testing scheduled to commence in the latter part of fiscal 2005.

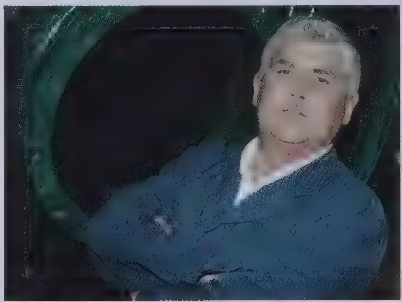
SELECTED ANNUAL INFORMATION

Years ended March 31	**2004**	**2003**	**2002**
(in thousands of dollars, except earnings per share)	**$**	$	$
Consolidated Statements of Income			
Revenue	**33,932**	26,319	25,821
Net income	**1,952**	756	1,836
Basic and diluted earnings per share	**$0.11**	$0.02	$0.11
Consolidated Balance Sheets			
Total assets	**26,467**	28,014	24,489
Long-term debt (excluding current portion)	-	3,929	1,181
Cash dividends declared	-	-	-

Management's Discussion and Analysis continued

As described in note 19 to the consolidated financial statements, freight amounts billed to customers are recorded as revenue, rather than netted against freight costs which are part of manufacturing and selling costs. The comparative consolidated financial statements have been reclassified to conform to this presentation. Accordingly, freight billed to customers of $861,000 (2003 - $821,000; 2002 - $711,000) is included in revenue.

In the second half of fiscal 2002, various upgrade and new installation programs in both the upstream and downstream sectors of the petroleum industry were deferred because of economic and political uncertainty, low commodity prices and merger and acquisition activity. This reduced level of activity in the petroleum industry, and many other industry sectors, continued into fiscal 2003, as economic and political uncertainty persisted. In the latter part of fiscal 2003 and throughout 2004, revenue increased as a result of strong activity in the downstream and upstream sectors of the petroleum industry, the growing market acceptance of new products introduced in recent years, and the acquisitions of Mocoat in May 2002 and Parabeam in September 2002.



Mario Carreiro, Production, Edmonton

Net income was negatively impacted in 2003 by losses incurred to integrate Mocoat and Parabeam into the overall liquid storage business, and in 2004 by the provision for impairment of the agreement receivable from Enviro. Amortization of deferred costs and intangible assets increased in 2004 and 2003 by more than $600,000 from 2002 with the acquisitions of Mocoat and Parabeam in 2003, as well as the assets of ZCL-USA, Inc. during 2002. The level of amortization will start to decrease by the end of fiscal 2005, as certain of these costs are fully amortized.

Total assets increased in 2003 primarily due to the acquisitions of Mocoat and Parabeam. The majority of the debenture was included in equity (2004 – nil; 2003 – nil; 2002 – $7.6 million), prior to repayment in September 2002 from the proceeds of the issue of common shares and warrants and long-term debt. All long-term debt was repaid in 2004.

"The Company has a continuous improvement program aimed at reducing costs and maximizing operational efficiency."

RESULTS OF OPERATIONS

Year Ended March 31, 2004 Compared to the Year Ended March 31, 2003

Revenue

Revenue was $33.9 million in 2004 compared to $26.3 million in 2003, an increase of over $7.6 million or 28.9%. Revenue increased due to the strong activity in the downstream and upstream sectors of the petroleum industry, as well as other traditional markets, and the Company's expanding line of products. These products, both new products introduced in recent years and additional products with the acquisitions of Mocoat and Parabeam, although relatively new to their markets and not as significant as the major products, continue to gain market acceptance and contribute to revenue.

Rana Thakur, Production, Edmonton

Revenue less manufacturing and selling costs

Revenue less manufacturing and selling costs increased to $8.0 million (23.5% of revenue) from $5.1 million in 2003 (19.6% of revenue). The increase is a result of the higher revenue in 2004, as well as 2003 amounts being low due to losses incurred by Mocoat and Parabeam as steps were taken to integrate these operations into the overall liquid storage business; the integration of these operations was largely completed by the end of 2003. The development of the tank lining technologies is continuing, and costs which meet the criteria established by the Canadian Institute of Chartered Accountants ("CICA") are deferred.

Overall manufacturing margins have been maintained at similar levels as last year, with production improvements and cost reductions offsetting the impact of increased input costs. The Company has a continuous improvement program aimed at reducing costs and maximizing operational efficiency. The initial ISO certification of two of the Company's production facilities, and the recent update to ISO 9001:2000, are part of this continuing program.

Management's Discussion and Analysis continued

Amortization

Amortization was $2.0 million for the year, approximately the same level as 2003.

Amortization has increased during the last two years as a result of deferred costs and intangible assets added with the acquisitions of Mocoat and Parabeam in 2003, and the assets of ZCL-USA, Inc. in 2002. These were key strategic acquisitions related to the tank lining products currently under further development, and to the proprietary three-dimensional glass fabric that is an integral part of the Company's manufactured and lining products. The overall level of amortization should start to decrease by the end of fiscal 2005, as certain of these costs are fully amortized.

Barbara Dworkowski, Accounting, Edmonton

Additional lining development costs were deferred this year, and will continue in fiscal 2005; however, these additional costs in 2005 are not anticipated to exceed $500,000 and will be amortized upon the commercial production of the lining products.

General and Administration

General and administration expenses increased by $329,000, from $1.5 million in 2003 to $1.9 million in 2004, but decreased as a percentage of revenue from 5.9% in 2003 to 5.5% in 2004. The increase was largely due to incentive amounts of approximately $200,000 accrued for management in accordance with employment contracts.

General and administration expenses have generally been reduced through restructuring and cost reduction efforts over the past several years. These costs will, however, increase as the Company grows, and processes are put in place relating to the requirements of current corporate governance developments.

Provision for Impairment of Agreement Receivable

During the year, a provision for impairment of the full amount of the agreement receivable from Enviro of $880,000 was recorded. As described in note 3 to the consolidated financial statements, Enviro has not made any payments under the agreement receivable since the fourth quarter of fiscal 2003, and due to current business conditions in the Philippines, has been unable to commit to a repayment schedule. The amounts and timing of future repayment, and the fair value of underlying security, net of expected costs of realization, cannot be estimated with reasonable reliability. All available courses of action continue to be pursued to collect the balance of the receivable or otherwise realize upon security.

"During fiscal 2004, all long-term debt was repaid, and the related deferred finance costs were written-off."

Financing charges

Financing charges were $370,000, approximately the same level as 2003. As described in note 8 to the consolidated financial statements, financing charges represent interest on short-term indebtedness, including bank fees and other charges, interest on long-term debt, foreign exchange losses and amortization of deferred finance costs.

Long-term debt was refinanced in September 2002 and, along with the equity placement at that time, proceeds were used to repay the debenture. During fiscal 2004, all long-term debt was repaid, and the related deferred finance costs were written-off. Interest on short-term indebtedness was lower in 2004 due to the improved cash position, and the other indebtedness in 2003 as outlined in note 14(b) to the consolidated financial statements. Foreign exchange losses of $12,000 (2003 – $29,000) were related to transactions denominated in foreign currencies and the translation of the financial statements of Parabeam.

Richard Whitford, Sales, Edmonton

Income taxes

The Company's effective tax rate was 32.1% in 2004 as compared to 41.1% in 2003. Income taxes were lower in 2004 due to a decrease in Canadian statutory rates, and recoveries of prior years' taxes of $145,000 (2003 – nil). Income taxes increased in 2004 by $15,000 (2003 – $50,000) due to the effect on future tax assets and liabilities of the reduction in tax rates.

Future income taxes relate primarily to the utilization of losses of prior years for tax purposes, and differences between financial reporting and tax bases of assets and liabilities. The Company has accumulated losses for tax purposes which may be carried forward to reduce taxable income in future years as described in note 11 to the consolidated financial statements. The potential income tax benefit of these losses has been recognized for accounting purposes.

Net Income and Earnings Per Share

Net income increased by $1.2 million, to a record $2.0 million from $756,000 in 2003. Basic and diluted earnings per share increased by $0.09, to $0.11 in 2004 from $0.02.

Debenture costs, net of tax, were deducted for purposes of determining the basic and diluted per share computations; earnings per share in 2003 were reduced by $0.03 as a result of these costs. The debenture was repaid in 2003 and these costs were eliminated.

The weighted-average number of common shares for basic earnings per share increased to 17,640,106 as compared to 13,909,486 in 2003, as a result of the issue of shares during fiscal 2003.

The effect for 2004 of dilutive share options in the fourth quarter was 48,041 (2003 – nil). Certain stock options were not included in the calculation of diluted shares as their exercise prices exceeded the average market share price for each of the years. The warrants were not included in the calculation of diluted shares as the market share prices were below the performance thresholds. The debenture was not included in the calculation of diluted shares in 2003 as the market share price was below the threshold conversion price of $3.00.

SUMMARY OF QUARTERLY RESULTS

Historically, the second and third fiscal quarters have the highest levels of activity, corresponding to the seasonality of the installation of underground liquid storage systems in Canada. This seasonality is expected to continue, but may diminish as the Company expands its product line into new markets.

Revenue in 2004 was higher than 2003 in each quarter, except for the second quarter where completion and shipment of a number of large orders were delayed to early in the third quarter. The first, third and fourth quarters of 2004 were each record quarters.

Quarterly Results

Years Ended March 31	Q1 Jun 30	Q2 Sep 30	Q3 Dec 31	Q4 Mar 31	Year
(in thousands of dollars, except per share amounts)	$	$	$	$	$
2004					
Revenue	7,409	7,896	10,726	7,901	33,932
Net income	236	97	1,134	485	1,952
Basic and diluted earnings per share	$0.01	$0.01	$0.06	$0.03	$0.11
2003					
Revenue	5,108	8,027	7,110	6,074	26,319
Net income	(93)	737	108	4	756
Basic and diluted earnings per share	($0.03)	$0.04	$0.01	$0.00	$0.02

"The Company considers that cash flow from operations, current credit facilities and other expected capital resources will allow the implementation of growth programs ..."

LIQUIDITY AND CAPITAL RESOURCES

The Company considers that cash flow from operations, current credit facilities and other expected capital resources will allow the implementation of growth programs, including development of new products and support of overall growth of operations, and other expected financial requirements. The Company has operating lines of credit of $10,250,000 provided by a chartered bank that are not utilized.

In May 2004, the Company announced the acquisition of the business assets of Durex Steel & Alloy Industries Ltd. ("Durex") for $1.0 million paid in cash on closing. In the event that other acquisitions are identified that are in the best interests of the Company, and meet strategic objectives, cash may also be raised through the issue of additional debt and shares.

Working capital (current assets less current liabilities) increased by over $1.4 million during the year to $10.1 million, as current assets increased by $1.3 million to $14.7 million at March 31, 2004, and current liabilities decreased by $100,000 to $4.6 million. This increase is related to the profitable operating results for the year and the repayment of long-term debt (elimination of current portion).

At March 31, 2004, accounts receivable increased by $259,000 or 4% to $6.4 million, inventory increased by $177,000 or 3% to $5.6 million, and accounts payable and accrued liabilities increased by $655,000 or 17% to $4.5 million. These are normal operating increases related to the higher level of activity in the fourth quarter of 2004 as compared to 2003. The Company deals largely with major oil and gas companies in Canada, performs ongoing credit evaluations and maintains allowances for potential doubtful accounts. No one customer generally makes up more than 10% of revenue, but at a particular point in time, depending on the timing of sales, there may be higher proportionate exposure in accounts receivable. At March 31, 2004, two customers accounted for 26% (2003 – one customer, 17%) of accounts receivable.

During the year, a provision of $880,000 was recorded for the impairment of the agreement receivable from Enviro. All available courses of action continue to be pursued to collect the balance of the receivable or otherwise realize upon security. Any collections will have a positive impact on income and cash.

Shareholders' equity increased to $20.9 million, as a result of net income for the year. At the Annual General and Special Meeting on August 18, 2003, shareholders passed a special resolution to eliminate the deficit at March 31, 2003 and reduce the stated capital of the Company. Accordingly, in the second quarter, contributed surplus was reduced by $745,000, share capital by $8.3 million, and accumulated deficit by $9.0 million.

Management's Discussion and Analysis continued

Cash Flows

Cash flows from operating activities increased by $2.7 million, to $6.1 million this year from $3.4 million in 2003, commensurate with the increase in income before non-cash items (amortization, provision for impairment of agreement receivable and future income taxes).

In 2004, long-term debt of $4.6 million was repaid, and $189,000 of common shares were repurchased under the normal course issuer bid ("NCIB"). In 2003, common shares and warrants of $7.0 million and long-term debt of $5.0 million were issued, and proceeds were used to repay the debenture and related costs, as well as all previous long-term debt.

During the second quarter, the Toronto Stock Exchange ("TSX") accepted notice of the NCIB filed by the Company. During the twelve-month period commencing July 10, 2003 and ending July 9, 2004, the Company may purchase on the TSX up to a maximum of 885,846 common shares, being approximately 5% of the issued and outstanding common shares. The actual number and timing of any purchases will be determined by the Company, and the price for any such shares will be the market price. The Company believed that its common shares were trading at a price range which did not adequately reflect their value in relation to the assets, business and future prospects. During the year, 222,000 common shares (2003 – nil) were repurchased for cancellation under the NCIB.

Property, plant and equipment additions in 2004 were $581,000 (2003 - $455,000). These additions related to leasehold and land improvements and equipment to increase production capacity and efficiency, and the upgrade of computer equipment. Development costs of $141,000, related to the development of lining materials and processes, were deferred in 2004 (2003 – nil). Lining development continues in fiscal 2005, and additional costs are not anticipated to exceed $500,000. In 2003, cash of $1.6 million, including bank indebtedness assumed, was used for the acquisitions of Mocoat and Parabeam.

Summary of Cash Flows

Years ended March 31	**2004**	2003
(in thousands of dollars)	**$**	$
Operating activities	**6,101**	3,435
Financing activities	**(4,832)**	(566)
Investing activities	**(722)**	(1,727)
Increase in cash	**547**	1,142
Cash, beginning of the year	**1,333**	191
Cash, end of the year	**1,880**	1,333

"Cash flows from operating activities increased by $2.7 million, to $6.1 million this year ..."

Contractual Obligations

The contractual obligations outlined below exclude ongoing purchase commitments in the normal course of business. The Company has no long-term purchase commitments relating to operations or capital expenditures.

During the year, all long-term debt was repaid. In 2003, long-term debt, excluding the current portion, increased to $3.9 million, as a result of the refinancing of bank term debt in September 2002.

Certain activities and requirements are financed through license agreements and operating leases. The Company has entered into long-term license arrangements which expire between October 2006 and December 2008. These agreements give the Company rights to manufacture and sell products in certain geographic areas utilizing the licensors' technology. As described in the table below and note 16 to the consolidated financial statements, the total undiscounted minimum royalty payments under these license agreements amounted to $2.0 million at March 31, 2004.

The Company leases certain of its premises and automotive, office and other equipment under long-term operating lease arrangements. As described in the table below and note 16 to the consolidated financial statements, the undiscounted minimum lease payments amounted to $1.4 million at March 31, 2004.

Government grants included in long-term liabilities on the balance sheet relate to government assistance received in prior years with respect to the purchase of property, plant and equipment. The Company has no obligation to repay the amounts or other contractual commitments with respect to the grants.

OFF-BALANCE SHEET ARRANGEMENTS

The Company has not entered into any off-balance sheet arrangements. License agreements and operating leases are included in contractual obligations above, and foreign exchange derivative arrangements are described in financial and other instruments below.

Contractual obligations

Payments Due by Year	**2005**	**2006-2007**	**2008-2009**	**2010-2014**	**Total**
(in thousands of dollars)	$	$	$	$	$
Long-term debt	--	--	--	--	--
License agreements	467	900	625	--	1,992
Operating leases	429	531	186	217	1,363
Total contractual obligations	896	1,431	811	217	3,355

Management's Discussion and Analysis continued

TRANSACTIONS WITH RELATED PARTIES

The related party transactions are described in note 14 to the consolidated financial statements. There are no ongoing contractual or other commitments resulting from these transactions.

FOURTH QUARTER

Historically, the first and fourth fiscal quarters have the lowest levels of activity, corresponding to the seasonality of the installation of underground liquid storage systems in Canada.

In the fourth quarter, revenue was a record $7.9 million this year, up by 30.1% from $6.1 million last year. Net income for the fourth quarter increased to $485,000 from $4,000 for the quarter last year. Basic and diluted earnings per share were $0.03 as compared to $0.00 for the fourth quarter last year. The increase this year was due to the higher revenue, plus a recovery of prior years' income taxes of $145,000, or $0.01 per share.

Cash flows from operating activities increased to $471,000, from cash used in operating activities of $1.0 million, as a result of the improved net income and the timing of cash collections and payments during the quarter.

OUTLOOK

To realize its vision, the Company must maintain its position in the Canadian marketplace, and pursue growth opportunities in related products and markets. Domestic and international markets for the Company's tank manufacturing and lining technologies will continue to be developed by leveraging customer relationships and innovative industry leadership. Continued success in reducing manufacturing costs and improving production processes will further enhance future profitability.

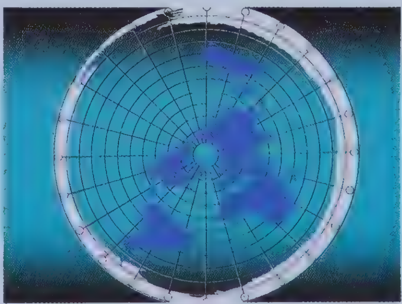
The Prezerver® system and other product innovations, such as the home heating oil above-ground tank, have a high level of industry acceptance. Utilizing similar technology and manufacturing expertise, a number of new products were recently successfully introduced into several market sectors. Additional products are under development, including double wall tank upgrade systems and aboveground products to compete in markets traditionally served only by steel tanks.

There is a very large and growing need for upgrading both underground and aboveground liquid storage, driven by environmental legislation and industry standards requiring secondary containment for storage of hazardous liquids. There are significant opportunities to establish ZCL's tank

"The Company is in a strong financial position and poised to grow both through internal expansion and acquisitions."

lining technologies as the preferred method of upgrading single wall tanks across North America. In conjunction with an alliance of major suppliers, the Company is developing and testing new lining materials and processes that will provide superior quality and performance and inherently safe installation techniques.

Subsequent to March 31, 2004, the Company acquired the business assets of Durex, a steel aboveground tank manufacturer. Aboveground storage systems are a significant portion of both the upstream (production) and downstream (retail) tank markets. This acquisition allows the Company to access the retail market which is served only by steel-based products. Tank manufacturing and lining operations can be expanded, and a full line of products can be offered to existing alliance customers as well as to new customers.



The Company is in a strong financial position and poised to grow both through internal expansion and acquisitions. Internal growth will come from introducing new products into existing markets, as well as expanding into new markets with existing products. While no acquisitions are on the immediate horizon, a number of specific opportunities have been identified to complement the Company's core business and expand into new markets.

The Company also has international opportunities for its technology and manufacturing expertise. A global strategy will be implemented by developing joint ventures with local partners. In the USA marketplace, the Company is moving forward with tank lining and aboveground tanks, such as home heating oil, aquaculture and other specialty tanks.

The Company's target is to grow revenue by 15% to 20% on an annual basis, with a corresponding increase in net income. With continued strength in primary markets, and growth of new products, the Company believes this target is an achievable goal. Future growth will largely come from tank lining and aboveground tank markets, including new steel products with the acquisition in May 2004, along with moderate continued growth in traditional underground markets. Actual growth each year will vary depending on economic and other conditions in various market sectors, and the Company's ongoing ability to deliver results and leverage its core competencies in technology, engineering and manufacturing.

Activity in the downstream and upstream sectors of the petroleum industry, as well as other traditional markets, picked up in the latter part of fiscal 2003 and was strong throughout 2004. Certain upgrade and new installation programs in both sectors of the petroleum industry were deferred in prior years due

Management's Discussion and Analysis continued

to uncertainty and mergers and acquisitions. With the robust level of activity in the petroleum sector, many companies are continuing to forecast major capital expenditures for the coming year.

The Company looks to growth in Canada, the USA and internationally, by utilizing its strong domestic base, customer alliances and industry leadership. Major oil companies are establishing global programs relating to procurement and standardization of specifications for their liquid storage systems, including the upgrade of existing tanks that otherwise may require costly replacement.

RISKS AND UNCERTAINTIES

In the normal course of business, the Company's operations are influenced by a number of internal and external factors, and exposed to risks and uncertainties, that can materially adversely affect its business, financial condition and operating results.

Aaron Sherman, Production, Nisku

Operations and Business Environment

The activities of the Company are subject to ongoing operational risks including the performance of key suppliers, product performance, proprietary technology and know-how, government and other industry regulations, successful integration of new acquisitions, dependence on key personnel, and reliance on information systems, all of which may affect the ability of the Company to meet its obligations. The ongoing ability to meet the needs of the marketplace is dependent on the development and introduction of new products and services. While management believes its innovation and technology make it a leader in the industry, revenue and results may be affected if products are not accepted in the marketplace, are not approved by regulatory authorities, or if products are not brought to market in a timely manner.

ZCL is engaged in competitive markets, subject to global economic and political influences and the financial strength of its customers. The Company is the leading manufacturer of fiberglass underground storage tanks in Canada, and its technology and products (high value-added complete liquid storage systems), operating structure, and professional customer service, differentiate it from its competitors. The primary market for ZCL's products continues to be the Canadian petroleum industry; expanding into global markets, and other markets beyond the petroleum industry, will minimize the dependency on any particular industry or economic sector.

Product Claims and Insurance

The Company manufactures and sells products that have a direct impact on the environment. Product failures could result in warranty and liability claims and the loss of customers. Correcting such failures or

> *"Each Prezerver® fuel storage system carries a $2 million insurance-backed warranty against pollution for a period of ten years."*

paying for such claims could require significant capital resources and have an adverse effect on operating results. The Company maintains high quality standards at its production facilities, uses only the most reputable suppliers for raw materials and other products, and has an unblemished history of no liability or warranty problems. ZCL also maintains insurance coverage for its operations, including general liability insurance. Each Prezerver® fuel storage system carries a $2 million insurance-backed warranty against pollution for a period of ten years. There is no guarantee that insurance will sufficiently cover all potential claims, or that adequate or any insurance can be obtained or maintained. Liability or claims may also arise that cannot be insured or management may choose not to insure due to high premiums or for other reasons.

Accounts Receivable and Credit

The Company carries a high level of accounts receivable on its balance sheet. Credit is spread among many customers and the Company has not experienced accounts receivable collection problems in the past. However, there is no assurance accounts receivable will be paid on a timely basis. Credit risk is described above and in note 15 to the consolidated financial statements. In addition, as described in note 3 to the consolidated financial statements, a provision for the full amount of the agreement receivable from Enviro was recorded during 2004.

Debt Availability and Interest Rate Risk

The Company requires ongoing working capital and financing to support operations and meet growth objectives. Long-term debt was repaid in full during 2004, and operating lines of credit are available but not utilized. While the Company has met all terms and covenants of these lending arrangements, there is no assurance that financing will continue to be available from this lender or alternative financial institutions on similar or any terms.

Foreign Exchange and Operations Risk

While the Company's operating results are reported in Canadian dollars, certain revenue and expenses are generated or incurred in other currencies, largely United States dollars and euros. Derivative financial instruments are used to manage a portion of the exposure to foreign exchange fluctuations. Substantially all business activities are currently carried out in Canada, but it is anticipated that exposure to, and fluctuation of, foreign currencies will be an ongoing risk in the future as the Company continues to expand into global markets.

A small portion of the Company's business is conducted through an integrated subsidiary in The Netherlands. This business involves risks associated with foreign political and legal jurisdictions and foreign suppliers and customers. The translation of the revenue, expenses and balance sheet accounts of these foreign operations will impact the Company's operating results and financial position.

Management's Discussion and Analysis continued

CRITICAL ACCOUNTING ESTIMATES

The Company's financial statements have been prepared following Canadian generally accepted accounting principles. The measurement of certain assets and liabilities is dependent upon future events whose outcome will not be fully known until future periods. Therefore the preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Such estimates and assumptions have been made using careful judgments, which in management's opinion, are within reasonable limits of materiality and conform to the significant accounting policies summarized in the consolidated financial statements. Actual results may vary from those estimated.

Tank Production, Edmonton

Property, Plant and Equipment, Deferred Costs, Intangible Assets and Goodwill

Property, plant and equipment, deferred costs, and intangible assets are recorded at cost less accumulated amortization. Goodwill is recorded at cost. The unamortized balances, or carrying values, are regularly reviewed for recoverability or tested for impairment whenever events or circumstances indicate that these amounts exceed their fair values. The valuation of these assets is based on estimated future net cash flows, taking into account current and future industry and other conditions. An impairment loss would be recognized if the carrying value exceeds the fair value.

The acquisitions of business assets are accounted for using the purchase method and the allocation of the purchase price relating to the purchases is completed in accordance with GAAP in Canada. This allocation results in values being assigned to assets acquired based on expected future cash flows using estimates, assumptions and other information available at the time of acquisition.

Amortization of property, plant and equipment, deferred costs, and intangible assets is based on estimates of the useful lives of the assets. The useful lives are estimated, and a method of amortization is selected, at the time the assets are initially acquired and then re-evaluated each reporting period.

Judgment is required to determine whether events or circumstances warrant a revision to the remaining periods of amortization. The estimates of cash flows used to assess the potential impairment of these assets are subject to measurement uncertainty. No impairment loss or write-down was required to be recognized in 2004 or 2003. A significant change in these estimates and judgments could result in a material change to amortization expense or impairment charges.

"The Company maintains high quality standards … uses only the most reputable suppliers … and has an unblemished history of no liability or warranty problems."

Warranties

The Company generally warrants its products for a period of one year after sale, and for up to thirty years for corrosion, if the products are properly installed and are used solely for storage of listed liquids. The Company's complete storage systems marketed under the Prezerver® trademark carry a ten-year, insurance-backed warranty covering product replacement and $2 million of third-party pollution protection. The Prezerver® warranty is covered by insurance underwritten by a major international insurer. A number of component materials and parts are similarly warranted by their manufacturers, thereby reducing the Company's exposure to warranty claims.

The Company provides for warranties based on a review of products and warranties taking into account the collective experience and history of the Company as to warranty claims on its products. The Company maintains high quality standards at its production facilities, uses only the most reputable suppliers for raw materials and other products, and has an unblemished history of no liability or warranty problems. There is no guarantee that insurance will sufficiently cover all potential claims, or that adequate or any insurance can be obtained or maintained. The actual costs of warranties may vary from those estimated, and the difference may be material.

Allowance for Doubtful Accounts

The Company carries a high level of accounts receivable on its balance sheet. Credit is spread among many customers and the Company has not experienced accounts receivable collection problems in the past. The Company performs ongoing credit evaluations and maintains allowances for doubtful accounts, based on the assessment of individual customer receivable balances, credit information, past collection history and the overall financial strength of customers. A change in these factors could impact the estimated allowance and the provision for bad debts recorded in the accounts.

Impairment of Agreement Receivable

During the year, a provision for impairment of the full amount of the agreement receivable from Enviro of $880,000 was recorded. As described in note 3 to the consolidated financial statements, Enviro has not made any payments under the agreement receivable since the fourth quarter of fiscal 2003, and due to current business conditions in the Philippines, has been unable to commit to a repayment schedule.

The provision for impairment was based on past experience, and the estimates of the amounts and timing of future repayment and the fair value of underlying security. All available courses of action continue to be pursued to collect the balance of the receivable or otherwise realize upon security. Actual experience may result in the collection of the agreement receivable and the recovery of all, or a portion, of the provision for impairment.

Management's Discussion and Analysis continued

Future Income Tax Assets

Future income tax assets are recognized for the benefits from tax losses and deductions when it is determined that it is more likely than not that the benefits would be realized. The Company considers such factors as the expected life of the losses, estimated future taxable income, and other characteristics and sources of realizing the benefits. A change in these factors could impact the estimated realization of the future income tax assets and the income tax expense of the Company.

CHANGES IN ACCOUNTING POLICIES INCLUDING INITIAL ADOPTION


Kheng Ly, Production, Edmonton

Stock-Based Compensation and Other Stock-Based Payments

There has been considerable discussion in the marketplace concerning the accounting for stock-based compensation and other stock-based payments. Effective April 1, 2002 the Company adopted the recommendations of the CICA with respect to these amounts. As permitted under those recommendations, the Company applied the change prospectively for new awards granted on or after April 1, 2002. The Company chose to recognize no compensation expense when share options and warrants were granted to employees and directors under plans with no cash or equity settlement features, and pro-forma net income and earnings per share are disclosed. As described in note 9 to the consolidated financial statements, in accordance with the fair value method of accounting for stock-based compensation and based on the weighted-average assumptions, compensation expense that would have been recorded for 2004 was $215,000 (2003 – $110,000) or $0.01 per share (2003 – $0.01 per share). Under the same conditions and assumptions, compensation expense of approximately $0.01 per share would be recorded in fiscal 2005.

Direct awards of shares to employees and non-employees are accounted for in accordance with the fair value method of accounting for stock-based compensation. In periods prior to April 1, 2002, the Company recognized no compensation when share options or warrants were issued to employees.

During the fourth quarter of the year ended March 31, 2004, the Company began expensing employee stock-based compensation and other stock-based payments in accordance with the amended recommendations of the CICA. The change was made with retroactive effect to April 1, 2003, for all employee stock-based compensation using the fair value method for all awards granted or modified on or after April 1, 2003. The fair value of share options and warrants at the date of grant is determined using an option pricing model and compensation expense is recognized over the vesting

"During the fourth quarter of the year ended March 31, 2004, the Company began expensing employee stock-based compensation and other stock-based payments ..."

period of the share options and warrants. As a result of this change, $10,000 has been recorded as compensation expense in 2004 (2003 – nil) with a corresponding increase in contributed surplus.

The Company has one share option plan and issued warrants as part of the private placement in September 2002. These options and warrants, including the number issued and expired, are described in note 9 to the consolidated financial statements.

Generally Accepted Accounting Principles

Effective April 1, 2003, the Company prospectively adopted the recommendation of the CICA with respect to Handbook Section 1100, Generally Accepted Accounting Principles ("GAAP"). This standard establishes what constitutes Canadian generally accepted accounting standards and provides guidance on the GAAP hierarchy. The adoption of this standard had no effect on the Company's financial position, results of operations or cash flows.

Impairment of Long-lived Assets

The new recommendations of the CICA with respect to impairment of long-lived assets were to be adopted for fiscal years beginning on or after April 1, 2003. The CICA encouraged earlier application, and the Company adopted these new recommendations effective April 1, 2002, whereby long-lived assets are tested for recoverability whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. An impairment loss is then recognized when the carrying amounts exceed their fair value. As recommended, the change was applied prospectively.

Long-lived assets of the Company include property, plant and equipment, intangible assets and deferred start-up costs. During 2004 and 2003, there were no events or changes in circumstances which indicated that the carrying amounts of long-lived assets may not be recoverable and no impairment loss was recognized.

FINANCIAL AND OTHER INSTRUMENTS

The consolidated financial statements are reported in Canadian dollars, including the results of an integrated foreign subsidiary. Certain transactions, revenue and expenses are generated or incurred in other currencies, largely United States dollars and euros. The exchange rate risk, on an annual basis, primarily reflects the impact of fluctuating exchange rates on the net difference between revenue, expenses and other transactions in each of the currencies.

Derivative financial instruments are used by the Company to manage a portion of its exposure to foreign exchange rate fluctuations. The Company's policy is not to utilize derivative financial instruments for trading or speculative purposes.

Management's Discussion and Analysis continued

The Company enters into foreign currency forward contracts, options and collars to pay for certain raw materials denominated in euros, provided by a foreign subsidiary. These derivative contracts, not accounted for as hedges, are marked to market, and any changes in the market value are recorded in income or expense when the changes occur. The fair value of these instruments is recorded as accounts receivable or payable.

At March 31, 2004, the Company had entered into foreign currency collar arrangements not accounted for as hedges. These arrangements provided for the purchase of euros, up to a total Canadian dollar equivalent of $1.5 million, at rates of $1.566 or $1.6175 per euro. The fair values of these arrangements, estimated using market rates at March 31, 2004, are nil (2003 – nil). During the year, net realized and unrealized gains of less than $5,000 (2003 – nil) relating to derivative financial instruments were recorded in financing charges.

Everlast™ Tank, Nisku

OTHER

Additional Information

Additional information relating to the Company, including the Annual Information Form (AIF), is filed on SEDAR at www.sedar.com

Outstanding Share Data

As at May 21, 2004, there are 17,511,320 common shares outstanding. No additional shares have been issued from March 31, 2004 to the date of this report.

Management Report

May 21, 2004

The Annual Report, including the consolidated financial statements, is the responsibility of the management of the Company. The consolidated financial statements were prepared by management in accordance with accounting principles generally accepted in Canada. When alternative accounting methods exist, management has chosen those it considers most appropriate in the circumstances. The significant accounting policies used are described in note 1 to the consolidated financial statements. The integrity of the information presented in the financial statements, including estimates and judgments relating to matters not concluded by year end, is the responsibility of management. Financial information presented elsewhere in this Annual Report has been prepared by management and is consistent with the information in the consolidated financial statements.

Management is responsible for the establishment and maintenance of systems of internal accounting and administrative controls which are designed to provide reasonable assurance that the financial information is accurate and reliable, and that the Company's assets are appropriately accounted for and adequately safeguarded.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities and for final approval of the annual consolidated financial statements. The Board appoints an Audit Committee consisting of unrelated, non-management directors that meets at least four times each year under a written mandate from the Board. The Audit Committee meets with management and with the independent auditors to satisfy itself that they are properly discharging their responsibilities, reviews the consolidated financial statements and the Auditors' Report, including the quality of the accounting principles and significant judgements applied, and examines other auditing and accounting matters. The Committee approves the terms of the engagement of the auditors, reviews the annual audit plan and the results of the audit, and recommends to the Board the firm of auditors to be appointed by the shareholders.

The consolidated financial statements have been reviewed by the Audit Committee and approved by the Board of Directors of ZCL Composites Inc. The consolidated financial statements have been examined by the shareholders' auditors, Ernst & Young LLP, Chartered Accountants. The Auditors' Report outlines the nature of their examination and their opinion on the consolidated financial statements of the Company. The independent auditors have full and unrestricted access to the Audit Committee, with and without management being present.

Venence G. Côté
President and
Chief Executive Officer

Tony G. Barlott
Vice President Finance
and Chief Financial Officer

Consolidated Financial Statements

Auditors' Report

To the Shareholders of
ZCL Composites Inc.

We have audited the consolidated balance sheets of ZCL Composites Inc. as at March 31, 2004 and 2003 and the consolidated statements of retained earnings (deficit), income, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at March 31, 2004 and 2003 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Ernst & Young LLP

Chartered Accountants

Edmonton, Canada
May 21, 2004

Consolidated Balance Sheets

As at March 31 (in thousands of dollars)	2004 $	2003 $
Assets		
Current		
Cash	**1,880**	1,333
Accounts receivable	**6,363**	6,104
Inventories *[note 2]*	**5,556**	5,379
Prepaid expenses	**188**	115
Future tax assets *[note 11]*	**699**	421
	14,686	13,352
Agreement receivable *[note 3]*	**—**	880
Property, plant and equipment *[note 4]*	**7,814**	7,981
Deferred costs *[note 5]*	**717**	1,579
Intangible assets *[note 6]*	**1,324**	1,748
Goodwill	**1,926**	1,926
Future tax assets *[note 11]*	**—**	548
	26,467	28,014
Liabilities and Shareholders' Equity		
Current		
Accounts payable and accrued liabilities	**4,525**	3,870
Income taxes payable	**35**	82
Current portion of long-term debt *[note 8]*	**—**	714
Future tax liabilities *[note 11]*	**27**	17
	4,587	4,683
Long-term debt *[note 8]*	**—**	3,929
Government grants	**160**	169
Future tax liabilities *[note 11]*	**838**	153
	5,585	8,934
Commitments *[note 16]*		
Shareholders' equity		
Share capital *[note 9]*	**18,853**	27,378
Contributed surplus *[note 9]*	**77**	745
Retained earnings (deficit)	**1,952**	(9,043)
	20,882	19,080
	26,467	28,014

See accompanying notes

On behalf of the Board:

Director

Director

Consolidated Statements of Retained Earnings (Deficit)

Years ended March 31 (in thousands of dollars)	2004 $	2003 $
Deficit, beginning of the year	(9,043)	(8,976)
Deficit elimination *[note 9]*	9,043	—
Net income for the year	1,952	756
Common share issue costs (2003 – net of tax of $186) *[note 9]*	—	(362)
Convertible subordinated debenture costs (2003 – net of tax of $237)	—	(461)
Retained earnings (deficit), end of the year	1,952	(9,043)

See accompanying notes

Consolidated Statements of Income

Years ended March 31 (in thousands of dollars)	2004 $	2003 $
Revenue *[note 3]*	33,932	26,319
Manufacturing and selling costs	25,966	21,171
	7,966	5,148
Amortization	1,968	1,948
General and administration	1,873	1,544
Provision for impairment of agreement receivable *[note 3]*	880	—
Financing charges *[note 8]*	370	372
Income before income taxes	2,875	1,284
Income taxes *[note 11]*		
Current	(42)	28
Future	965	500
	923	528
Net income for the year	1,952	756
Basic and diluted earnings per share *[note 12]*	$0.11	$0.02

See accompanying notes

Consolidated Statements of Cash Flows

Years ended March 31 (in thousands of dollars)	2004 $	2003 $
Cash Flows from Operating Activities		
Cash receipts from customers	**33,996**	26,492
Cash paid to suppliers and employees	**(27,714)**	(22,646)
Interest paid	**(176)**	(367)
Income taxes paid	**(5)**	(44)
	6,101	3,435
Cash Flows from Financing Activities		
Repayment of long-term debt	**(4,643)**	(3,276)
Repurchase of common shares for cancellation *[note 9]*	**(189)**	—
Issue of long-term debt	**—**	5,000
Finance costs	**—**	(209)
Issue of common shares and warrants	**—**	7,000
Common share issue costs	**—**	(548)
Repayment of convertible subordinated debenture	**—**	(8,185)
Convertible subordinated debenture costs	**—**	(348)
	(4,832)	(566)
Cash Flows from Investing Activities		
Purchase of property, plant and equipment	**(581)**	(455)
Deferred development costs *[note 5]*	**(141)**	—
Collection of agreement receivable *[note 3]*	**—**	366
Business acquisitions, including bank indebtedness assumed *[note 13]*	**—**	(1,638)
	(722)	(1,727)
Increase in cash	**547**	1,142
Cash, beginning of the year	**1,333**	191
Cash, end of the year	**1,880**	1,333

See accompanying notes

Notes to Consolidated Financial Statements

March 31, 2004 and 2003

1. Significant Accounting Policies

ZCL Composites Inc. (the "Company") manufactures and distributes liquid storage systems, including fiberglass underground and aboveground storage tanks and related products and accessories. The Company's financial statements have been prepared following Canadian generally accepted accounting principles. The measurement of certain assets and liabilities is dependent upon future events whose outcome will not be fully known until future periods. Therefore the preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Actual results may vary from those estimated.

In particular, the amounts recorded for amortization of property, plant and equipment, deferred costs and intangible assets are based on estimates of the remaining useful lives of such assets. Furthermore, the provision for warranty claims and the impairment of the agreement receivable are based on past experience and the most currently available information regarding warranty costs and the collectibility of the agreement receivable. These estimates, and those related to the cash flows used to assess the potential impairment of property, plant and equipment, deferred costs, intangible assets, and goodwill are subject to measurement uncertainty and the impact on the financial statements of future periods could be material. Such estimates and assumptions have been made using careful judgments, which in management's opinion, are within reasonable limits of materiality and conform to the significant accounting policies summarized below:

Basis of presentation

The consolidated financial statements include the accounts of ZCL Composites Inc. and its wholly-owned subsidiary companies, LeGay Fiberglass (1993) Limited, Mocoat Services Incorporated, and Parabeam Industries BV (Netherlands). All significant intercompany transactions and balances have been eliminated in the preparation of these consolidated financial statements.

Inventories

Raw materials are valued at the lower of cost, determined on an average cost basis, and replacement cost. Work in progress and finished goods are valued at the lower of manufacturing cost and net realizable value on a specific item basis. Manufacturing cost includes the cost of raw material, direct labour costs, and applicable production overheads.

Notes to Consolidated Financial Statements continued

March 31, 2004 and 2003

1. Significant Accounting Policies (continued)

Property, plant and equipment

Property, plant and equipment are recorded at cost less accumulated amortization. Amortization is computed using the declining balance method at the following annual rates:

Buildings	4%
Land improvements	10%
Manufacturing equipment	10%
Office equipment	20%
Automotive equipment	30%

Amortization of leasehold improvements is computed using the straight-line method over the term of the lease.

Deferred development costs

The Company expenses research and development costs. Certain development costs are deferred when criteria established by the Canadian Institute of Chartered Accountants with respect to development costs are met, and amortized over future periods commencing with commercial production of the product or process.

Deferred development costs are amortized on a straight-line basis over the estimated expected life of the related products. All costs are currently being amortized over five years.

Unamortized deferred development costs are regularly reviewed for recoverability, based on projections of future revenues less relevant costs. The unamortized amount is written-off when the criteria for deferral are no longer met or written-down when the unamortized balance exceeds the amounts of deferred costs that can be reasonably regarded as recoverable.

Deferred start-up and finance costs

Deferred start-up and finance costs are recorded at cost less accumulated amortization. Amortization is computed using the straight-line method over the following periods:

Deferred start-up costs	5 years
Deferred finance costs	term of loan agreements

Deferred finance costs are amortized over periods ranging from three to five years.

Intangible assets

Intangible assets with finite lives are recorded at cost less accumulated amortization. Amortization is computed using the straight-line method over the following periods:

Licenses	term of licensing agreements
Non-patented technology	estimated expected life of related products

Licenses are amortized over periods ranging from eight to twenty years. Non-patented technology is amortized over five years.

Impairment of long-lived assets

Long-lived assets of the Company include property, plant and equipment, deferred start-up costs and intangible assets. These assets are tested for recoverability whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. An impairment loss is then recognized when the carrying amounts exceed their fair value.

During the years, there were no events or changes in circumstances which indicated that the carrying amounts of long-lived assets may not be recoverable and no impairment loss was recognized.

Goodwill

Goodwill is recorded at cost. The carrying value is tested for impairment annually and when events or circumstances occur that would indicate that this amount may be impaired. An impairment loss would be recognized if the carrying value exceeds the fair value.

Warranties

The Company generally warrants its products for a period of one year after sale, and for up to thirty years for corrosion, if the products are properly installed and are used solely for storage of listed liquids. The Company's complete storage systems marketed under the Prezerver trademark carry a ten-year, insurance-backed warranty covering product replacement and $2 million of third-party pollution protection. The Prezerver warranty is covered by insurance underwritten by a major international insurer. A number of component materials and parts are similarly warranted by their manufacturers, thereby reducing the Company's exposure to warranty claims.

The Company provides for warranties based on a review of products and warranties taking into account the collective experience and history of the Company as to warranty claims on its products.

Notes to Consolidated Financial Statements continued

March 31, 2004 and 2003

1. Significant Accounting Policies (continued)

Government grants

Government grants relating to property, plant and equipment are recorded as a deferred credit and are being amortized on the same basis as the property, plant and equipment to which they relate.

Derivative financial instruments

Derivative financial instruments are used by the Company to manage a portion of its exposure to foreign exchange rate fluctuations. The Company's policy is not to utilize derivative financial instruments for trading or speculative purposes.

The Company enters into foreign currency forward contracts, options and collars to pay for certain raw materials denominated in euros, provided by a foreign subsidiary. These derivative contracts, not accounted for as hedges, are marked to market, and any changes in the market value are recorded in income or expense when the changes occur. The fair value of these instruments is recorded as accounts receivable or payable.

Foreign currency translation

Transactions denominated in a foreign currency and financial statements of an integrated foreign subsidiary included in the consolidated financial statements are translated as follows: monetary items at the rate of exchange in effect at the balance sheet dates; non-monetary items at historical exchange rates; revenue and expense items at average exchange rates that produce substantially the same amounts that would have resulted had the transactions been translated on the dates they occurred; and amortization of assets at the same historical exchange rates as the assets to which they relate. Any resulting exchange gains or losses are included in income in the period incurred.

Revenue recognition

Revenue is recorded upon change of ownership, which normally occurs at the time of shipment of the product. In circumstances where the customer chooses to temporarily store goods on the Company's premises, revenue is recognized upon manufacturing completion.

Income taxes

The Company uses the liability method to account for income taxes. Under this method, future income tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities, and measured using the substantively enacted tax rates and laws that will be in effect when the differences are expected to reverse.

Earnings per share

Basic earnings per share is computed based on the weighted average number of common shares outstanding during the year. Diluted earnings per share is computed using the treasury stock method, which assumes that the cash that would be received on the exercise of options, warrants and the convertible debenture is applied to purchase shares at the average price during the period and that the difference between the shares issued upon their exercise and the number of shares obtainable under this computation, on a weighted average basis, is added to the number of shares outstanding. Antidilutive amounts are not considered in computing diluted earnings per share.

Changes in accounting policies

a) Stock-based compensation

Effective April 1, 2002 the Company adopted the recommendations of the Canadian Institute of Chartered Accountants with respect to stock-based compensation and other stock-based payments. As permitted under those recommendations, the Company applied the change prospectively for new awards granted on or after April 1, 2002. The Company chose to recognize no compensation expense when share options and warrants were granted to employees and directors under plans with no cash or equity settlement features. Pro-forma net income and earnings per share reflecting share options and warrants granted in fiscal year 2003 are disclosed in note 9 using the fair value method. Direct awards of shares to employees and non-employees are accounted for in accordance with the fair value method of accounting for stock-based compensation. In periods prior to April 1, 2002, the Company recognized no compensation when shares, stock options or warrants were issued to employees.

During the fourth quarter of the year ended March 31, 2004, the Company began expensing employee stock-based compensation and other stock-based payments in accordance with the amended recommendations of the Canadian Institute of Chartered Accountants. The change was made with retroactive effect to April 1, 2003, for all employee stock-based compensation using the fair value method for all awards granted or modified on or after April 1, 2003. The fair value of share options and warrants at the date of grant is determined using an option pricing model and compensation expense is recognized over the vesting period of the share options and warrants. As a result of this change, $10,000 has been recorded as compensation expense in 2004 with a corresponding increase in contributed surplus.

The Company has one share option plan, which is more fully described in note 9.

Notes to Consolidated Financial Statements continued

March 31, 2004 and 2003

1. Significant Accounting Policies (continued)

b) Generally accepted accounting principles

Effective April 1, 2003, the Company prospectively adopted the recommendation of the Canadian Institute of Chartered Accountants with respect to Handbook Section 1100, Generally Accepted Accounting Principles ("GAAP"). This standard establishes what constitutes Canadian generally accepted accounting standards and provides guidance on the GAAP hierarchy. The adoption of this standard had no effect on the Company's financial position, results of operations or cash flows.

2. Inventories

(in thousands of dollars)	**2004** **$**	**2003** **$**
Raw materials	**2,685**	2,159
Work in progress	**236**	290
Finished goods	**2,635**	2,930
	5,556	5,379

3. Agreement Receivable

Effective January 1, 2001, the Company sold its 40% interest in ZCL Enviro Systems, Inc. ("Enviro"), a corporation incorporated under the laws of the Philippines, for $760,000. At that time, the Company had certain trade accounts receivable due from Enviro and Enviro agreed to pay the combined balance plus interest in instalments by June 30, 2003.

No payments have been received from Enviro since the fourth quarter of fiscal 2003. Due to business conditions in the Philippines, Enviro has been unable to commit to a repayment schedule. The amounts and timing of future repayment, and the fair value of underlying security, net of expected costs of recovery, cannot be estimated with reasonable reliability. Accordingly, during the year, a provision for impairment of $880,000 was recorded.

The Company will continue to pursue all available courses of action to collect the balance of the receivable or otherwise realize upon its security. As collateral for the agreement receivable, the Company is entitled to the return of its 40% interest in Enviro, which manufactures products under a long-term license agreement utilizing the Company's technology.

(in thousands of dollars)	$
Proceeds receivable from sale of interest	760
Accounts receivable	903
Balance due – January 1, 2001	1,663
Additional amounts invoiced	365
Payments received	(782)
Agreement receivable – March 31, 2002	1,246
Payments received	(366)
Agreement receivable – March 31, 2003	880
Provision for impairment	(880)
Agreement receivable – March 31, 2004	—

Revenue includes nil (2003 – $65,000) from Enviro, and accounts receivable at March 31, 2004 include nil (2003 – $7,000) due from Enviro.

4. Property, Plant and Equipment

	2004		2003	
(in thousands of dollars)	Cost $	Accumulated amortization $	Cost $	Accumulated amortization $
Land	293	—	293	—
Buildings	2,876	865	2,852	782
Leasehold and land improvements	279	87	168	75
Manufacturing equipment	10,326	5,588	10,029	5,081
Office equipment	1,405	911	1,261	801
Automotive equipment	165	79	160	43
	15,344	7,530	14,763	6,782
Net book value	7,814		7,981	

Amortization expense includes $748,000 (2003 – $730,000) for the amortization of property, plant and equipment and $9,000 (2003 – $25,000) for the amortization of government grants.

Notes to Consolidated Financial Statements continued

March 31, 2004 and 2003

5. Deferred Costs

	2004		2003	
(in thousands of dollars)	Cost $	Accumulated amortization $	Cost $	Accumulated amortization $
Deferred development costs	**2,831**	**2,114**	2,690	1,421
Deferred start-up costs	**707**	**707**	707	595
Deferred finance costs	**213**	**213**	213	15
	3,751	**3,034**	3,610	2,031
Net book value		**717**		1,579

Deferred development costs include $141,000 (2003 – $nil) incurred during the year. These costs relate to development projects in process at March 31, 2004 and were not amortized during the year. The total amount of research and development charged to expense for the year is not separately identifiable, as such costs are only tracked for development projects that are deferred.

Amortization expense includes $693,000 (2003 – $712,000), $112,000 (2003 – $140,000), and $198,000 (2003 – $18,000) for the amortization of deferred development costs, start-up costs and finance costs respectively. Deferred finance costs were written-off during the year as the related financing was repaid.

6. Intangible Assets

	2004		2003	
(in thousands of dollars)	Cost $	Accumulated amortization $	Cost $	Accumulated amortization $
Licenses	**521**	**396**	521	361
Non-patented technology	**1,944**	**745**	1,944	356
	2,465	**1,141**	2,465	717
Net book value		**1,324**		1,748

Amortization expense includes $35,000 (2003 – $35,000) for the amortization of licenses and $389,000 (2003 – $356,000) for non-patented technology.

7. Bank Indebtedness

The Company has operating lines of credit of $10,250,000 provided by a chartered bank that are not utilized. These lines of credit are payable on demand and bear interest at prime rate plus 0.25% (4.25%; 2003 – 5.00%). The operating lines of credit contain certain restrictive covenants including the maintenance of certain financial ratios and limitations on capital expenditures and additional debt. The Company has pledged as collateral a general security agreement, guarantees of subsidiaries, and a pledge of inventory under section 427 of the Bank Act.

8. Long-term Debt

(in thousands of dollars)	2004 $	2003 $
Bank term loan bearing interest at prime rate plus 0.50%, payable in quarterly instalments of $178,572 plus interest with the remaining balance due in September 2005; the interest rate applied at March 31, 2003 was 5.25%.	—	4,643
Less current portion	—	714
	—	3,929

Financing charges

(in thousands of dollars)	2004 $	2003 $
Interest, long-term	154	189
Interest, short-term	6	136
Foreign exchange losses	12	29
Amortization of deferred finance costs *[note 5]*	198	18
	370	372

9. Share Capital, Contributed Surplus and Stock-based Compensation

(a) Share capital

Authorized

Unlimited number of common shares

Issued and outstanding

	2004		2003	
(in thousands of dollars)	Shares #	$	Shares #	$
Balance, beginning of the year	17,716,920	27,378	9,295,866	20,078
Reduction of stated capital (i)	—	(8,298)	—	—
Repurchased under normal course issuer bid (ii)	(222,000)	(240)	—	—
Issued to employees under employee recognition program (iii)	16,400	13	—	—
Issued for cash under private placement (iv)	—	—	7,368,422	6,300
Issued for acquisition *[note 13]*	—	—	1,052,632	1,000
Balance, end of the year	17,511,320	18,853	17,716,920	27,378

(i) At the Annual General and Special Meeting of Shareholders on August 18, 2003, the shareholders approved the reduction of the stated capital of the Company. Accordingly, contributed surplus was reduced by $745,000, share capital by $8,298,000, and accumulated deficit by $9,043,000.

Notes to Consolidated Financial Statements continued

March 31, 2004 and 2003

9. Share Capital, Contributed Surplus and Stock-based Compensation (continued)

(a) Share Capital (continued)

(ii) During the year, 222,000 common shares were repurchased for cancellation pursuant to a normal course issuer bid at a cost of $189,000. As a result of these repurchases, share capital was reduced by $240,000 and contributed surplus was increased by $51,000.

(iii) In March 2004, 16,400 common shares were issued to employees as recognition for the Canada's 50 Best Managed Companies award received by the Company. As a result of this direct award of shares to employees, share capital and compensation expense of $13,000 were recorded.

(iv) In September 2002, the Company completed a private placement to ARC Energy Venture Fund 3 of 7,368,422 units ("Unit") at $0.95 per Unit for total cash proceeds of $7,000,000. Each Unit was comprised of one common share and 0.5 Performance Warrants (see Warrants below). Of the total cash proceeds, $700,000 was attributed to the value of the Performance Warrants, as computed using an option pricing model, and allocated to contributed surplus. Issue costs of $548,000, net of tax of $186,000, were charged to deficit.

(b) Share options

Under the Company's share option plan, options to purchase common shares may be granted by the Board of Directors to directors, officers, employees, and persons who provide management or consulting services to the Company. The plan has no cash or equity settlement features. As part of the private placement in September 2002, the Company agreed that the maximum term of options would be no greater than five years, the exercise price would not be less than the price received by the Company upon the completion of the most recent offering of common shares, the total number of options would be no more than 10% of the issued and outstanding common shares, and the options would vest one-third per year, commencing on the first anniversary of the date the option is granted.

At the Annual General and Special Meeting of Shareholders on August 19, 2002, the shareholders authorized the number of options under the plan at 1,500,000 common shares. As part of the approval of the issue of the common shares under the employee recognition program, the Toronto Stock Exchange required that the number of options under the plan be reduced by 16,400, which was the number of common shares issued.

The Company has issued 1,145,000 (2003 – 1,185,000) of these options, which expire on dates between March 2006 and September 2007. The following table presents the changes during the years and the options outstanding:

	2004		2003	
	Shares #	Weighted Average Exercise Price $	Shares #	Weighted Average Exercise Price $
Balance, beginning of the year	1,185,000	0.99	180,000	2.28
Issued	125,000	0.95	1,100,000	0.95
Expired	(165,000)	1.05	(95,000)	3.00
Balance, end of the year	1,145,000	0.97	1,185,000	0.99

	2004			
	Options Outstanding		Options Exercisable	
Exercise Price $	Shares #	Weighted Average Remaining Contractual Life in Years	Shares #	Weighted Average Exercise Price $
1.35	70,000	1.93	70,000	1.35
0.95	1,075,000	3.59	341,667	0.95
0.95 – 1.35	1,145,000	3.49	411,667	1.02

(c) Warrants

As part of the private placement in September 2002, the Company issued 3,684,211 Performance Warrants ("Warrant"). One-half of these Warrants were segregated, and approved by the shareholders at the Annual General and Special Meeting of Shareholders on August 18, 2003, for transfer to senior management of the Company. Each Warrant entitles the holder to subscribe for one common share at a price of $0.95 for a period of up to five years subject to a performance vesting provision. The Warrants vest at one-third intervals upon the weighted-average trading price of common shares reaching thresholds, for a period of twenty trading days, of $1.90, $2.85 and $3.80 per common share.

The 550,000 warrants associated with the convertible subordinated debenture, at a weighted average exercise price of $2.47, expired in November 2002.

(d) Stock-based compensation

The Black–Scholes model, used by the Company to calculate the values of options and warrants, as well as other currently accepted option valuation models, were developed to estimate the fair value of freely-tradeable, fully-transferable options and warrants without vesting restrictions. Such options and warrants differ significantly from the share options and warrants granted by the Company. These models require subjective assumptions, including future share price volatility and expected time until exercise, which affect the calculated values. Accordingly, management believes that these models do not necessarily provide a reliable single measure of the fair values of the share options and warrants granted by the Company.

Notes to Consolidated Financial Statements continued

March 31, 2004 and 2003

9. Share Capital, Contributed Surplus and Stock-based Compensation (continued)

(d) Stock-based compensation (continued)

Share options and warrants granted on or after April 1, 2003

The Company uses the fair value method of accounting for all share options and warrants granted to employees on or after April 1, 2003. During the year, the Company granted 50,000 share options and 150,000 warrants, all of which were granted with exercise prices in excess of the market share price on the grant date. Stock-based compensation expense of $10,000 (2003 – nil) was recognized during the year.

The following estimated fair values of these options and warrants were determined, at the date of the grants, using the Black–Scholes option pricing model with the following weighted-average assumptions:

	Share Options	Warrants
Weighted-average fair value	$0.29	$0.18
Risk-free interest rate (%)	3.89	4.37
Expected hold period to exercise (years)	4.0	4.5
Volatility in the price of Company's shares (%)	60.8	60.5
Dividend yield (%)	0.0	0.0

In addition, during the year, 75,000 share options were issued to a non-employee as consideration for consulting services. In accordance with the fair value method of accounting for stock-based compensation for non-employees, $16,000 (2003 – nil) was recorded as contributed surplus and an expense in the statement of income.

Share options and warrants granted in 2003

The fair value of share options and warrants granted in 2003, all of which were granted with exercise prices in excess of the market share price on the grant date, were determined, at the date of grants, using the Black–Scholes option pricing model. The following table provides the required pro-forma measures of net income and earnings per share had compensation expense been recognized based on the fair value, as at the date of the grant, of the options and warrants granted to employees in 2003, in accordance with the fair value method of accounting for stock-based compensation:

(in thousands of dollars)	2004 $	2003 $
Net income for the year	**1,952**	756
Stock-based compensation expense	**215**	110
Pro-forma net income for the year	**1,737**	646

	2004 $	2003 $
Earnings per share:		
Reported basic and diluted earnings per share	**0.11**	0.02
Compensation expense per share	**0.01**	0.01
Pro-forma basic and diluted earnings per share	**0.10**	0.01

The following estimated fair values of these options and warrants were determined using the following weighted-average assumptions:

	Share Options	Warrants
Weighted-average fair value	$0.37	$0.38
Risk-free interest rate (%)	4.0	4.0
Expected hold period to exercise (years)	4.0	5.0
Volatility in the price of the Company's shares (%)	61.6	56.2
Dividend yield (%)	0.0	0.0

10. Convertible Subordinated Debenture

During 1998, the Company received $11,000,000 under a convertible subordinated debenture bearing interest at 9.75%. The debenture, plus an amount accruing daily sufficient to generate to the lender an additional rate of return of 8.25% per annum was due on November 30, 2002. The debenture, and any interest payable, were convertible with 120 days notice to common shares of the Company at the Company's option, at any time after May 1, 2002. The conversions were at a price per share equal to the twenty-day weighted average trading price of the shares on the Toronto Stock Exchange, providing that the price was greater than $3.00.

In 1999 and 2000, the Company repaid $5,500,000 of the debenture. In May 2002, the Company agreed to make monthly payments of $100,000, and in September 2002, the debenture was repaid in full. A make-whole premium based on the present value, over the period remaining to maturity of the debenture, of the difference between the debenture interest rate of 9.75% and the lender's reinvestment rate of return, was payable on amounts repaid. No make-whole premium was payable on the monthly repayments made between May 2002 and September 2002. A make-whole premium on the repayment of the debenture in September 2002 of $56,000 was paid. Warrants to purchase 550,000 common shares of the Company that were issued in connection with the debenture, expired on November 30, 2002.

Notes to Consolidated Financial Statements continued

March 31, 2004 and 2003

11. Income Taxes

The Company's effective income tax expense has been determined as follows:

(in thousands of dollars)	**2004** **$**	2003 $
Statutory federal and provincial taxes	**1,019**	510
Increase (decrease) in income taxes resulting from:		
Recovery of prior years' taxes	**(145)**	—
Manufacturing and processing allowance	**(33)**	(75)
Impact of changes in tax rates	**15**	50
Non-deductible expenses and other items	**67**	43
	923	528

Significant components of the Company's future tax assets and liabilities are as follows:

(in thousands of dollars)	**2004** **$**	2003 $
Future tax assets		
Loss carryforwards	**739**	1,986
Share issue costs	**107**	149
Tax basis of development costs in excess of carrying values	**419**	318
Other	**137**	101
	1,402	2,554
Future tax liabilities		
Carrying value of property, plant and equipment and intangible assets in excess of tax basis	**1,566**	1,666
Other	**2**	89
	1,568	1,755
	(166)	799
Represented by:		
Future tax assets – current	**699**	421
Future tax assets – long-term	**—**	548
Future tax liabilities – current	**(27)**	(17)
Future tax liabilities – long-term	**(838)**	(153)
	(166)	799

The Company has accumulated losses for Canadian tax purposes of approximately $2,142,000 which may be carried forward and used to reduce taxable income in future years.

The Canadian tax losses available for carryforward must be claimed in years ending no later than:

(in thousands of dollars)	$
2006	69
2007	505
2008	18
2009	119
2010	1,431

The potential income tax benefit associated with these losses has been recognized for accounting purposes.

12. Earnings Per Share

The following table sets forth the net income available to common shareholders and weighted-average number of common shares outstanding for the computation of basic and diluted earnings per share:

(in thousands of dollars)	2004 $	2003 $
Numerator:		
Net income for the year	1,952	756
Convertible subordinated debenture costs, net of tax	—	(461)
Net income available to common shareholders for basic and diluted earnings per share	1,952	295
Denominator:		
Weighted-average shares for basic earnings per share	17,640,106	13,909,486
Effect of dilutive share options (1,025,000)	48,041	—
Adjusted weighted-average shares for diluted earnings per share	17,688,147	13,909,486

Certain share options are not included in the calculation of diluted shares as their exercise prices exceeded the average market share price for each of the years. The warrants are not included in the calculation of diluted shares as the market prices were below the performance threshold. The convertible subordinated debenture is not included in the calculation of diluted shares in 2003 as the market share price was below the threshold conversion price of $3.00.

Notes to Consolidated Financial Statements continued

March 31, 2004 and 2003

13. Acquisitions

In May 2002, the Company acquired 100% of the shares of Mocoat Services Inc., an Alberta-based corporation that provides corrosion prevention services to the oil and gas industry in Western Canada and manufactures a proprietary tank lining or internal secondary containment system.

In September 2002, the Company acquired 100% of the shares of Parabeam Industries BV, which is based in The Netherlands and manufactures a three-dimensional glass fabric that is used by the Company in the manufacture of double wall tanks and tank lining products.

The acquisitions were accounted for using the purchase method and the consolidated financial statements include the results of operations from the purchase dates. The aggregate consideration given, including acquisition costs, has been allocated to the fair value of the net assets acquired and liabilities assumed, including those relating to the relocation of certain operations to new premises, as follows:

(in thousands of dollars)	2003 $
Cash consideration	**1,375**
Common share consideration *[note 9]*	**1,000**
Aggregate purchase price	**2,375**
Assets and liabilities acquired at fair values:	
Bank indebtedness assumed	**(263)**
Non-cash working capital	**827**
Property, plant and equipment	**1,305**
Non-patented technology	**1,944**
Long-term debt	**(1,007)**
Future tax liability	**(431)**
Net assets acquired	**2,375**

14. Related Party Transactions

a) Trucking services of $352,000 (2003 – $318,000) were provided by a corporation controlled by a director of the Company. Accounts payable and accrued liabilities at March 31, 2004 included $6,000 (2003 – $4,000) owing to the corporation. Normal commercial rates were paid for these services.

b) During 2003, as part of the approval of the acquisition of Mocoat Services Inc., the convertible subordinated debenture holder required that the Company raise additional capital, subordinated to their position, in the amount of $550,000. Certain directors of the Company loaned the $550,000 to the Company in May 2002. The loans were unsecured, bore interest at the annual rate of 25% per annum, and were repaid in September 2002. Interest of $58,000 was paid to the directors relating to these loans and included in interest on short-term indebtedness.

15. Financial Instruments and Risk Management

Financial instruments

The fair value of accounts receivable, accounts payable and income taxes payable approximate their carrying values, due to the relatively short periods to maturity of these instruments. The fair value of long-term debt at March 31, 2003 approximated its carrying value due to interest rates which reflected market rates.

Foreign currency risk management and derivative financial instruments

The consolidated financial statements are reported in Canadian dollars, including the results of an integrated foreign subsidiary. Certain transactions, revenue and expenses are generated or incurred in other currencies, largely United States dollars and euros. The exchange rate risk, on an annual basis, primarily reflects the impact of fluctuating exchange rates on the net difference between revenue, expenses and other transactions in each of the currencies. Substantially all business activities are currently carried out in Canada, but it is anticipated that this will be a continuing risk in the future as the Company continues to expand into global markets.

At March 31, 2004, the Company had entered into foreign currency collar arrangements not accounted for as hedges. These arrangements provided for the purchase of euros, up to a total Canadian dollar equivalent of $1.5 million, at rates of $1.566 or $1.6175 per euro. The fair values of these arrangements, estimated using market rates at March 31, 2004, are nil (2003 – nil). During the year, net realized and unrealized gains of less than $5,000 (2003 – nil) relating to derivative financial instruments were recorded in financing charges.

Interest rate risk management

All long-term debt was repaid during the year, and the convertible subordinated debenture was repaid in 2003.

Credit risk management

The maximum exposure to credit risk is represented by the carrying amount of the accounts receivable and agreement receivable. A provision for impairment of the full amount of the agreement receivable has been recorded as described in note 3. The credit risk related to accounts receivable results from the possibility of customers defaulting on payment of these accounts. The Company deals largely with major oil and gas companies in Canada, and performs ongoing credit evaluations and maintains allowances for potential doubtful accounts. No one customer generally makes up more than 10% of revenue, but at a particular point in time, depending on the timing of sales, there may be higher proportionate exposure in accounts receivable. At March 31, 2004, two customers accounted for 26% (2003 – one customer, 17%) of accounts receivable.

Notes to Consolidated Financial Statements continued

March 31, 2004 and 2003

16. Commitments

License agreements

The Company has license agreements which expire between October 2006 and December 2008. The agreements give the Company exclusive rights to manufacture and sell products in certain geographic areas utilizing the licensors' technology.

These license agreements provide for the payment of royalties based on revenues from related products during the license terms. Aggregate minimum royalty payments under these license agreements are as follows:

(in thousands of dollars)	$
2005	**467**
2006	**467**
2007	**433**
2008	**380**
2009	**245**
	1,992

Operating leases

The minimum annual rentals under the terms of operating leases for premises and for automotive, office and other equipment are as follows:

(in thousands of dollars)	$
2005	**429**
2006	**298**
2007	**233**
2008	**124**
2009	**62**
Thereafter	**217**
	1,363

17. Segmented Information

Operating segments are defined as components of the Company for which separate financial information is available that is evaluated regularly by the chief operating decision maker in allocating resources and assessing performance. The chief operating decision maker of the Company is the Chief Executive Officer.

The Company operates in one reportable segment, which is the manufacture and distribution of liquid storage systems including fiberglass underground and aboveground storage tanks and related products and accessories.

Information about products

Providing information relating to revenue from external customers for each product, or group of similar products, is impractical and accordingly, only total revenue has been presented in the statements of income.

Information about geographic areas

	Revenues		Property, plant and equipment and goodwill	
(in thousands of dollars)	**2004** **$**	2003 $	**2004** **$**	2003 $
Canada	**32,436**	25,291	**8,934**	9,046
Foreign countries	**1,496**	1,028	**806**	861
	33,932	26,319	**9,740**	9,907

Revenue is attributed to the geographic area based on location of the Company's operations. No revenue attributed to any individual foreign country is material. The property, plant and equipment relating to foreign countries are located in The Netherlands.

Information about major customers

The Company has long-term contracts and alliance arrangements with many of the major oil and gas companies in Canada. The top seven customers (of which four were the same in 2004 and 2003) accounted for approximately 38% (2003 – 38%) of revenue, with the largest customer making up 11% (2003 – 10%) of revenue.

18. Subsequent Event

Subsequent to March 31, 2004, the Company acquired the business assets of Durex Steel & Alloy Industries Ltd. ("Durex") located in Edmonton, Alberta. Durex manufactures steel aboveground storage tanks. The purchase price was $1,000,000 paid in cash on closing.

19. Comparative Figures

The comparative consolidated financial statements have been reclassified from statements previously presented to conform to the presentation of the current consolidated financial statements. In the current year, freight amounts billed to customers are recorded as revenue, rather than netted against freight costs which are recorded as part of manufacturing and selling costs. Accordingly, freight billed to customers of $861,000 (2003 – $821,000) is included in revenue.

Corporate Information

Board of Directors
James S. Edwards, Chairman of the Board
Venence G. Côté, Director, President and CEO
Fred J. Dyment, Director
Roderick W. Graham, Director
Simon Sochatsky, Director

Transfer Agent and Registrar
Olympia Trust Company
#2300, 125 - 9th Avenue S.W.
Calgary, Alberta
T2G 0P6

Annual General Meeting
1:00 pm on August 16, 2004
at The Westin Edmonton
10135 - 100 Street, Edmonton, Alberta

Auditors
Ernst & Young LLP
1801 Scotia 2
Scotia Place
10060 Jasper Avenue
Edmonton, Alberta
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Corporate Office
6907 - 36 Street
Edmonton, Alberta
Canada T6B 2Z6

General Counsel
Parlee McLaws LLP
Suite 1500, Manulife Place
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Edmonton, Alberta
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Common Shares Outstanding
as of May 21, 2004
Total Outstanding: 17,511,320

Investor Relations
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Stock Listing and Share Symbol
Toronto Stock Exchange: **ZCL**

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